Restructure Korea's Electric Power Industry

1. Summary:

The Korean National Assembly passed the legislation to begin the process of restructuring of the electric power industry in December 2000. Currently, the state-owned Korea Electric Power Corporation (KEPCO) dominates the domestic electric power industry. Since KEPCO covers approximately 95 percent (47,053 MW) of the national total power generation capacity as of June 2000, the restructuring of Korean electric power industry provides the potential for significant opportunities. As the National Assembly passed the relevant legislation in December 2000, the Ministry of Commerce, Industry and Energy (MOCIE) unveiled its plan to privatize KEPCO in January 2001. As the first step, the Board of Directors of KEPCO, on February 23, 2001, voted to divide its power plants into six Generation subsidiaries (Gencos) by April 2, 2001, when the power generation competition will begin. This report provides an update on the proposed restructuring plan, and recent developments. Considering KEPCO's total power generation capacity, CS Korea believes that this restructuring process will provide U.S. companies with excellent business opportunities to enter into the Korean market.

2. Legislation passed by the National Assembly to privatize KEPCO:

After a one year delay, as a result of domestic political considerations, the National Assembly passed the legislation to commence the electric power industry restructuring in Korea on December 8, 2000. This legislation was essential to begin the restructuring process to establish separate Gencos of KEPCO that will be sold to introduce competition in electric power market.

The legislation consists of:

- Promotion of Restructuring Electric Power Industry Act: To provide the legal basis to divide KEPCO's generation sector to establish several Gencos.

- Electricity Business Act: To establish 'Power Exchange', 'Electricity Committee', and to introduce competition among generation, transmission, and distribution companies.

3. The Electric Power Industry Restructuring Plan:

The Electric Power Industry Restructuring Plan released by MOCIE in January 2001 includes:

- **Genco privatization:**

KEPCO's six Gencos (one nuclear and five thermal Gencos) and a power pool system will be established by April 2, 2001 to introduce competition in the power generation sector. KEPCO announced the six Genco presidents on March 22, 2001. These presidents will run each Genco for three years which will compete within an established power pool system. After a one-year grace period to assess the possibility of real competition, the thermal Gencos will begin to be privatized in 2002. The asset value of each thermal Genco is estimated at approximately US$ 2.5 billion with an average power generation capacity of 7,600 MW. However, the nuclear Genco, with the asset value of US$ 14 billion and power generation capacity of 18,251 MW, will remain under KEPCO and government control for safety and national security reasons. The hydro power plants will not be privatized and will be included in the nuclear Genco. The detailed plan will be finalized by the first half, 2001.

	President	Power generation capacity (MW)	Employee (total: 34,306)
Namdong Genco	Haeng-Soon Yoon	7,165	1,589
Joongboo Genco	Bong-Il Kim	7,738	1,937
Seoboo Genco	Moon-Sin Hong	7,946	1,606
Namboo Genco	Im-Taek Lee	7,710	1,767
Dongseo Genco	Sang-Yung Lee	7,500	1,866
Nuclear Genco	Yang-Woo Choi	18,251	6,167
Post - KEPCO *	Soo-Byung Choi	-	19,150
Power Exchange	Vacant	-	224

* Industry term for KEPCO after spin off 6 Gencos and Power Exchange.

- **Subsidiaries privatization:**

In addition, KEPCO announced on February 28, 2001, the sale of shares in two subsidiaries, the Korea Plant Service & Engineering Co. Ltd. (KPS) and the Korea Power Engineering Co., Inc. (KOPEC). KPS is a power plant maintenance company with an estimated asset value of $220 million and a sales volume of $340 million. KOPEC is a power plant design and engineering company with an estimated asset value of $150 million and a sales volume of $170 million. The two subsidiaries are being sold on the basis of competitive public tender. The deadlines for bidding application are April 3, 2001 (KPS) and April 10, 2001 (KOPEC).

- **Disco privatization:**

MOCIE is developing plans to divide KEPCO's distribution sector into 12 distribution companies (Discos) and sell them to private investors by the first half of 2002. The total asset value of KEPCO's distribution sector is estimated at US$ 10 billion, and KEPCO's 10 thousand employees, 30 percent of the total, work in this sector. MOCIE will finalize the Disco privatization plan by the first half, 2001.

4. Remaining Issues:

Although MOCIE is expected to accelerate the KEPCO privatization, some issues still remain:

- **The value of the Gencos**

KEPCO estimates the asset value of each non-nuclear Genco at US$ 2.5 billion and that of nuclear Genco at US$ 14 billion. However, foreign and domestic potential buyers may have doubts about the assessed value of the Gencos. Although the Korean power industry restructuring committee recommended to MOCIE in May 2000 to privatize the first Genco through stock sale (30 percent through IPO and 70 percent through competitive bidding), the gap on the Gencos' estimated asset values remains a potential issue. Industry sources say the market value of Gencos will hinge on the regulation and rules of the Korean government on the future electric power market.

- **Return on Investment (ROI)**

The gap between the ROI estimated by KEPCO and expected by industry is potentially another contentious issue. Currently, KEPCO's ROI is approximately 10 percent, while the foreign bidders expect to receive at least a 15 percent ROI. This was also a significant issue during the sale of the Anyang & Puchon Combined Heat and Power Plants in 2000.

- **Debt**

The huge debt of KEPCO is still controversial. As of 1999, KEPCO has debt of US$ 28.2 billion. Gencos will assume the domestic debt, while foreign and short-term debt will remain within KEPCO. The domestic debt will be divided into each Genco in proportionate to the asset value. However, KEPCO and six Gencos will still be jointly responsible for the whole debt until Gencos sold to private investors. If KEPCO or any Genco can not repay its own debt, the other companies will be responsible to pay for it. Once privatized, the Gencos may not be jointly responsible for the whole debt any more, and the creditors may raise concerns about the weakening joint liabilities. In addition, the foreign creditors may default and request refund of the debt.

- **Retirement cost**

As of December 1999, KEPCO has 34,607 employees, but KEPCO will still have 34,306 employees after the Gencos are set up as described in the above table. However, as is often the case with the privatization, potential buyers predict up to 30 percent employee reduction for each Genco after privatization. KEPCO provides no on-going pension and medical insurance to the retired employees, and the Gencos will not inherit any obligation to the retired staff. However, the retirement benefits to the future retired Genco employees may be an issue. Market players want to reflect the retirement cost into their bidding price, which KEPCO does not. This factor may widen the gap of the Gencos' estimated value.

5. CS Korea Comment:

According to the 'Basic Plan for Restructuring of the Electricity Supply Industry' released by MOCIE in January 1999, MOCIE will spin off KEPCO into power generation, transmission, distribution sectors, and will privatize them. At the same time, competition will be introduced in the electric power industry through three phases: competition in the generation sector by 2002, wholesale competition by 2009, and retail competition after 2009. Although some parts of the KEPCO privatization plan remain, CS Korea believes that this restructuring trend in Korea will provide U.S. companies with good business opportunities. After considering opinion from interested parties, the Korean government will finalize the Genco / Disco privatization plan by the first half 2001. CS Korea will trace the development of these plans, and recommend U.S. companies to keep focusing on this process.

(Source: U.S. Commercial Service, Seoul, South Korea)